



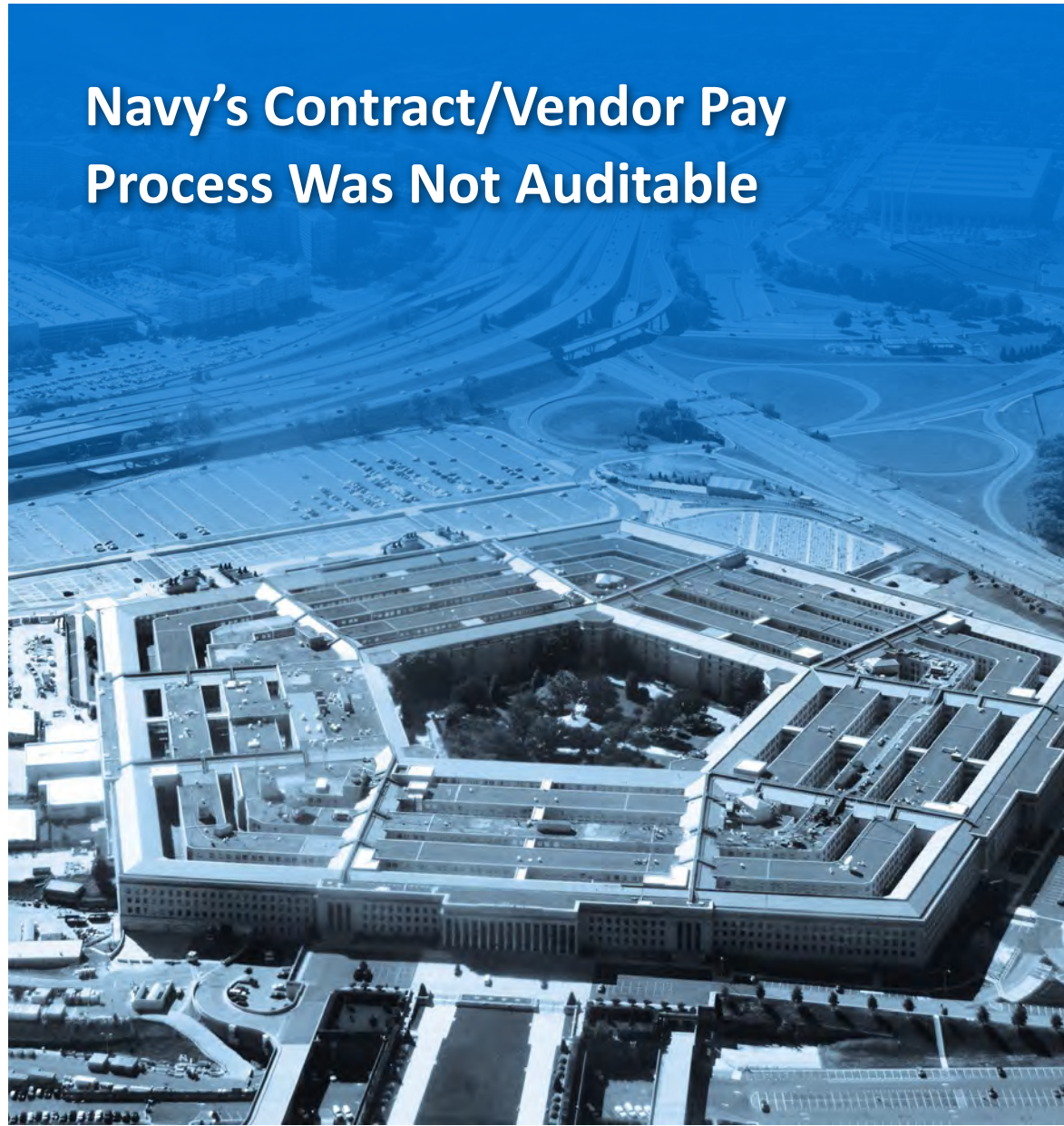
# INSPECTOR GENERAL

*U.S. Department of Defense*

JULY 1, 2015



## Navy's Contract/Vendor Pay Process Was Not Auditable



INTEGRITY ★ EFFICIENCY ★ ACCOUNTABILITY ★ EXCELLENCE

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# Results in Brief

## *Navy's Contract/Vendor Pay Process Was Not Auditable*

July 1, 2015

### Objective

Our objective was to determine whether the Navy's Contract/Vendor Pay (CVP) transactions were auditable and supported.

### Finding

We determined that the Navy could not provide an auditable CVP universe. Specifically,

- Navy Office of Financial Operations (FMO) could not compile a complete CVP universe. This occurred because Navy FMO did not design its financial management systems to identify CVP transactions and support an audit of CVP. In addition, Navy FMO did not perform detailed reconciliations of its CVP transactions; and
- The Naval Air Systems Command did not process Navy Enterprise Resource Planning CVP transactions timely. This occurred because Navy FMO did not develop its business processes to follow generally accepted accounting principles and record a liability when a good or service was received.

In addition, the Naval Facilities Engineering Command (NAVFAC) lacked appropriate supporting documentation for 17 of the 30 transactions nonstatistically reviewed. This occurred because NAVFAC did not develop procedures to ensure that personnel could support these transactions.

If Navy FMO cannot identify a complete CVP universe, which it reported as part of the "outlays" and "obligations incurred" line items on the Schedule of Budgetary

### Finding (cont'd)

Activity (SBA), there is an increased risk that the Navy will not produce an auditable universe of transactions for its SBA audit. Also, the Accounts Payable balance on the Navy's General Fund Balance Sheet may be understated. Lastly, the lack of support increased the risk that transactions were not valid and the financial statements were inaccurate. As the Navy moves forward with its audit readiness efforts, determining that the financial statements contain all necessary transactions will be a key part of the financial statement audits.

The Under Secretary of the Navy asserted that its SBA was audit ready based on assertions of business segments, including CVP. The deficiencies we identified in this report highlight specific challenges that should be corrected to improve the likelihood of a successful audit. If these deficiencies are not corrected, the Navy SBA audit opinion could be negatively affected.

### Recommendations

We recommend that the Deputy Assistant Secretary of the Navy (Financial Management and Comptroller) develop a reconciliation process that supports the current SBA and other financial statements; develop a process or system interface between Navy Enterprise Resource Planning and legacy systems to ensure transactions are processed in compliance with guidance; and establish procedures to identify and retain supporting documentation for all transaction types.

### Management Comments and Our Response

Comments from the Deputy Assistant Secretary of the Navy (Financial Operations), responding for the Assistant Secretary of the Navy (Financial Management and Comptroller), addressed Recommendation 1 and partially addressed the specifics of Recommendation 2 and 3. We request comments in response to the recommendations by July 31, 2015. Please see the Recommendations Table on the back of this page.

## ***Recommendations Table***

| Management   | Recommendations<br>Requiring Comment | No Additional<br>Comments Required |
|--|--------------------------------------|------------------------------------|
| Deputy Assistant Secretary of the Navy (Financial<br>Management and Comptroller) | 2, 3                                 | 1                                  |

Please provide Management Comments by July 31, 2015.





**INSPECTOR GENERAL  
DEPARTMENT OF DEFENSE  
4800 MARK CENTER DRIVE  
ALEXANDRIA, VIRGINIA 22350-1500**

July 1, 2015

MEMORANDUM FOR UNDER SECRETARY OF DEFENSE (COMPTROLLER)/  
CHIEF FINANCIAL OFFICER,  
DOD DIRECTOR, DEFENSE FINANCE AND ACCOUNTING SERVICE  
NAVAL INSPECTOR GENERAL

SUBJECT: Navy's Contract/Vendor Pay Process Was Not Auditable  
(Report No. DODIG-2015-142)

We are providing this report for review and comment. We considered management comments on a draft of this report when preparing the final report. We determined that the Navy could not provide an auditable Contract/Vendor Pay universe, and 17 of 30 transactions for the Naval Facilities Engineering Command were not supported. In addition, the Accounts Payable balance on the Navy's General Fund Balance Sheet may be understated because the Navy did not process its Enterprise Resource Planning transactions timely. The deficiencies identified in this report highlight specific challenges that should be corrected to improve the likelihood of a successful audit. If these deficiencies are not corrected, the Navy Schedule of Budgetary Activity audit opinion could be negatively affected. We conducted this audit in accordance with generally accepted government auditing standards.

DoD Instruction 7650.03 requires that recommendations be resolved promptly. Comments from the Deputy Assistant Secretary of the Navy (Financial Operations) addressed Recommendation 1 and partially addressed the specifics of Recommendation 2 and 3. Therefore, we request additional comments on Recommendations 2 and 3. We request all comments by July 31, 2015.

Please send a PDF file containing your comments to [audclev@dodig.mil](mailto:audclev@dodig.mil). Copies of your comments must have the actual signature of the authorizing official for your organization. We cannot accept the /Signed/ symbol in place of the actual signature. If you arrange to send classified comments electronically, you must send them over the SECRET Internet Protocol Router Network (SIPRNET).

We appreciate the courtesies extended to the staff. Please direct questions to me at (703) 601-5945.

A handwritten signature in blue ink that reads "Lorin T. Venable".

Lorin T. Venable, CPA  
Assistant Inspector General  
Financial Management and Reporting

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## Acronyms and Abbreviations

# Introduction

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## Objective

The audit objective was to determine whether Navy's Contract/Vendor Pay (CVP) transactions<sup>1</sup> were auditable and supported.

We adjusted our audit scope because Navy Office of Financial Operations (FMO) could not provide a complete CVP transaction universe. The CVP universe provided by Navy FMO included other transactions<sup>2</sup> that were not CVP. These other transactions should not have been included in our CVP universe and Navy personnel were not able to compile a CVP-only universe. However, we continued the audit to provide useful feedback to the Navy. We selected a sample of transactions to test for supportability from the CVP universe, regardless of the transaction type. Appendix A provides a discussion on the scope and methodology related to the revised objective.

## Background

Public Law 111-84<sup>3</sup> requires DoD financial statements to be audit ready by September 30, 2017. According to the Secretary of Defense,<sup>4</sup> DoD is required to achieve audit readiness for all DoD Statements of Budgetary Resources by the end of FY 2014. To meet audit readiness, the Department grouped business processes into four waves:

- appropriations received;
- Statements of Budgetary Resources audit;
- mission critical assets; and
- full financial statement audit.

However, DoD limited the scope of the Statements of Budgetary Resources audits to only current year appropriation activity and transactions, referred to as a Schedule of Budgetary Activity (SBA). This approach allows DoD Components to focus on mission critical tasks while they continue to build towards full financial statement auditability by FY 2017.

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<sup>1</sup> Transactions for Contract Pay and Vendor Pay.

<sup>2</sup> Non-CVP transactions included: Reimbursable Work Order; Foreign National Labor; Supervision, Inspection, and Overhead; and Transportation of Things transactions.

<sup>3</sup> Public Law 111-84, "National Defense Authorization Act of 2010," Subtitle A, Section 1003, October 28, 2009.

<sup>4</sup> Secretary of Defense memorandum, "Improving Financial Information and Achieving Audit Readiness," October 13, 2011.

The Navy's strategy to meet the Secretary of Defense requirement was an incremental approach to test internal controls and transactions, which would result in sustainable and repeatable processes to maintain audit readiness. The Navy's approach also grouped transactions and processes with similar attributes into 'segments' to support auditability.

The November 2013 FIAR guidance defines auditability as management's ability to assert that its financial statements, a financial statement line item, or a process are free of material misstatement. In addition, sufficient control activities and adequate documentation exist to undergo an examination or a financial statement audit. CVP is identified as a segment to support the Navy's goal to achieve audit readiness of its SBA.

The Navy defined the following terms.<sup>5</sup>

- **CVP segment**—the significant financial management processes, procedures, transactions, and accounting events needed to complete the procurement activities through contracting actions or vendor payments (or both) made to obtain goods or services (or both).
- **Contract Pay transactions**—include government-issued contracts for goods and services.
- **Vendor Pay transactions**—include government commercial purchase card program, training, and tuition payments.

The Navy used three systems to process CVP transactions at the U.S. General Ledger account level:

- Standardized Accounting and Reporting System–Field Level (STARS-FL);
- Standardized Accounting and Reporting System–Headquarters Claimant Module (STARS-HCM); and
- Navy Enterprise Resource Planning (Navy ERP).

The detail from the Navy's CVP transactions processed through STARS-FL, STARS-HCM, and Navy ERP were consolidated into the Navy's financial statements, including the Navy's SBA. The Navy's CVP transactions were included in the SBA line-item "outlays" and "obligations incurred," and were not separately reported.

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<sup>5</sup> The Navy defined these terms in the "Department of the Navy General Fund Contract/Vendor Pay: Audit Readiness Assertion Summary", April 15, 2014.



The Navy's management asserted CVP audit ready as of April 15, 2014. The Navy stated in its assertion CVP transactions were materially complete and supported by system records, based on results of data reconciliation analytics.

### ***Navy Office of Financial Operations***

Navy FMO, under the Deputy Assistant Secretary of the Navy (Financial Operations), is responsible for Navy financial and accounting activities. Navy FMO provides program oversight and conducts activities that are designed to improve the Navy's financial performance. Navy FMO also directs and oversees audit response activity between the Navy commands, service providers, and auditors.

### **Review of Internal Controls**

DoD Instruction 5010.40, "Managers' Internal Control Program Procedures," May 30, 2013, requires DoD organizations to implement a comprehensive system of internal controls that provides reasonable assurance that programs are operating as intended and to evaluate the effectiveness of the controls. We identified internal control weaknesses in the Navy's CVP auditability and supportability. We found that the Navy did not have controls in place to provide an auditable CVP universe; support some CVP transactions with adequate documentation; and consistently process CVP transactions in Navy ERP in accordance with generally accepted accounting principles. We will provide a copy of the final report to the senior official responsible for internal controls in the Navy.

## Finding

### Contract/Vendor Pay Was Not Auditable and Some Transactions Lacked Support

The Navy's CVP universe was not auditable. Specifically,

- Navy FMO could not compile a complete CVP universe. This occurred because Navy FMO did not design its financial management systems to identify CVP transactions<sup>6</sup> and support an audit of CVP. In addition, Navy FMO did not perform detailed reconciliations of its CVP transactions. If Navy FMO cannot identify a complete CVP universe, which is reported as part of the "outlays" and "obligations incurred" line items on its SBA, there is an increased risk that the Navy will not produce an auditable universe of transactions for its SBA audit; and
- Naval Air Systems Command (NAVAIR) did not process Navy ERP CVP transactions timely. This occurred because Navy FMO did not develop Navy ERP business processes to record a liability when a good or service was received as prescribed by generally accepted accounting principles. As a result, the Accounts Payable balance on the Navy's General Fund Balance Sheet may be understated.

As the Navy moves forward with its audit readiness efforts, determining that the financial statements contain all necessary transactions will be a key part of the financial statement audits.


In addition, the Naval Facilities Engineering Command (NAVFAC) did not support 17 of 30 transactions that we nonstatistically selected from STARS-FL. NAVFAC could not support its transactions because it did not have procedures in place to maintain supporting documentation. As a result of these unsupported transactions, there is an increased risk that transactions are not valid and the financial statements are inaccurate.

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<sup>6</sup> The CVP universe provided by the Navy included CVP and other types of transactions.

## Contract/Vendor Pay Universe Was Not Auditable

Contrary to the Navy's assertion, Navy FMO could not compile or verify a complete CVP universe.<sup>7</sup> According to Navy FMO officials, the Navy's financial management systems were not designed to identify and support business segments, including CVP. For example, the CVP universe compiled by Navy FMO inappropriately included other transactions that were not part of the CVP segment such as:



Navy FMO could not compile or verify a complete CVP universe.

- Reimbursable Work Order;
- Foreign National Labor;
- Supervision, Inspection, and Overhead; and
- Transportation of Things.

Navy FMO could not verify whether the CVP universe was complete because they did not perform all necessary detailed reconciliations from the three general ledger systems that processed CVP transactions. Navy FMO stated detailed reconciliations of CVP transactions between feeder systems and Navy ERP, STARS-FL, and STARS-HCM were beneficial because it would validate the CVP universe was complete and accurate.

Without a reconciled universe of transactions, Navy FMO cannot ensure that all CVP transactions are included in the CVP universe. In addition, Navy FMO cannot verify that financial statement reported balances are accurate if non-CVP transactions are erroneously included in the universe. If the balances are not fully reconciled, the likelihood of a successful audit is negatively affected because determining that the financial statements contain all the relevant transactions is a key part of a financial statement audit. However, Navy FMO did not perform any CVP reconciliations for Navy ERP. This occurred because Navy FMO officials stated significant manual efforts would be required to perform CVP reconciliations for Navy ERP, or the Navy ERP system would have to be re-coded.

For the STARS-FL and STARS-HCM systems, Navy FMO completed only 5 of 15 CVP reconciliations needed for the general ledger systems. Navy FMO stated they did not complete the CVP reconciliations because of the significant differences between the feeder-level systems<sup>8</sup> and STARS-FL and STARS-HCM. For example, a CVP reconciliation from a feeder system to STARS-FL included 161,585 differences that

<sup>7</sup> Completeness as defined by the AICPA is management's assertion that all transactions that should have been recorded were recorded in the accounting records. In this case it means that all CVP transactions that should have been included in the universe are present and transactions that are not CVP are excluded from the universe.

<sup>8</sup> Section 185, Title 10, United States Code states that a Feeder system is an automated or manual system from which information is derived for a financial management system or an accounting system.

totaled approximately \$864 million. Navy FMO indicated that manual efforts to research and determine whether a transaction was CVP were not cost effective because the reconciliations would not be required for the Navy's SBA audit.

Navy FMO stated future CVP reconciliations would not be required for the Navy's SBA audit because the SBA will be audited by line item, not by business segment like CVP. Navy FMO's assertion that CVP was auditable was inaccurate because Navy FMO could not reconcile the CVP unique transactions. We agree that a segmented universe of only CVP reconciled transactions is not needed for the audit of the "outlays" and "obligations incurred" lines reported on the SBA. However, if Navy FMO cannot compile a complete CVP universe, there is an increased risk that the Navy cannot reconcile its outlays and obligations incurred line items, which may negatively impact the Navy's ability to produce an auditable universe for its SBA audit. The "outlays" and "obligations incurred" universes are critical to the success of the SBA audit. *The Deputy Assistant Secretary of the Navy (Financial Operations) should develop a reconciliation process that is based on detail-level transaction data from Department of the Navy's general ledger systems that supports lines on the current Schedule of Budgetary Activity and other financial statements that the Navy may assert as audit ready. (Recommendation 1)*

## Business Processes Not Developed to Recognize Liabilities Timely

NAVAIR did not process Navy ERP CVP transactions timely, which resulted in delayed liability recognition.

NAVAIR did not process Navy ERP CVP transactions timely, which resulted in delayed liability recognition. We tested 30 transactions for supportability from Navy ERP. See Appendix A for further discussion of our sampling methodology. We determined that all 30 transactions were properly supported; however, NAVAIR did not recognize the liability in its general ledger prior to the contractor submitting an invoice in all 30 transactions.

If liabilities are not recognized in the correct period, the likelihood of a successful audit is negatively affected because the completeness of the financial statements is a key part of a financial statement audit.

The Statement of Federal Financial Accounting Standards 1 (SFFAS 1)<sup>9,10</sup> states that when an entity accepts title to goods, whether the goods are delivered or in transit, the entity should recognize a liability for the unpaid amount of the goods. The

<sup>9</sup> SFFAS 1 "Accounting for Selected Assets and Liabilities," March 30, 1993.

<sup>10</sup> The Navy uses DoD Regulation 7000.14-R, "DoD Financial Management Regulation," volume 4, chapter 9 to implement the requirements of SFFAS 1, "Accounting for Selected Assets and Liabilities," March 30, 1993.

average delay between the invoice date and liability posting was 23 days, and the longest delay was 89 days. In one example, the invoice was received 21 days before the liability was recorded for a transaction, totaling \$63,110. See Appendix B for details of the delay between the liability recognition and invoice receipt dates identified in Navy ERP.

Navy FMO did not develop its business processes so that Navy ERP recognized liabilities in accordance with SFFAS 1. NAVAIR personnel stated the liability recognition delay was a limitation in the Navy ERP system because the system did not interface with wide area workflow (WAWF).<sup>11</sup> Instead, Navy officials stated that Navy ERP followed a systematic process to recognize the liability in its general ledger. First, contractor personnel created an invoice in WAWF, which was sent through the entitlement system. Navy ERP then validated the invoice to the payment and accounting pre-validation systems to ensure that the invoice matched an existing obligation. After the transaction was approved in the accounting pre-validation system, Navy ERP recorded it, and it was recognized as a liability in the general ledger.

Navy FMO personnel stated that delays with the liability recognition could occur several weeks after an invoice was received. The delays could be caused by any of the following:

- the obligation was not posted in Navy ERP;
- receipt and acceptance in WAWF may not be done timely;
- invoice could be rejected in WAWF; or
- missing goods receipt or invoice receipt for services or missing invoice receipt for goods.

As a result, the Navy may record transactions in the wrong period, causing the Accounts Payable balance on its General Fund Balance Sheet to be understated. In addition, cutoff tests<sup>12</sup> performed by auditors on future financial statements may reveal this weakness, which could impact auditability of the Accounts Payable balance. *The Deputy Assistant Secretary of the Navy (Financial Operations) should develop a process or system interface between Navy ERP and WAWF that processes transactions timely and in compliance with Statement on Federal Financial Accounting Standards 1, "Accounting for Selected Assets and Liabilities." (Recommendation 2)*

<sup>11</sup> WAWF is the DoD's required, web-based system for receipt and acceptance and electronic invoicing.

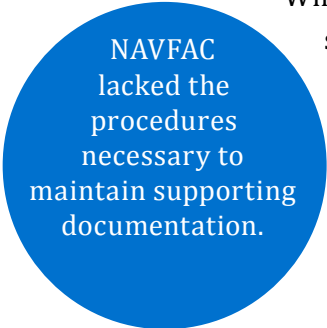
<sup>12</sup> A cutoff test determines if transactions are recorded in the proper period.



## Documentation Not Available For Some NAVFAC Transactions

NAVFAC did not support 17 of the 30 transactions selected from STARS-FL.<sup>13</sup> We tested 30 transactions from each of the three systems that processed CVP transactions.<sup>14</sup> NAVAIR and Office of Naval Research supported each of their 30 transactions from Navy ERP and STARS-HCM, respectively. See Appendix A for further discussion of our sampling methodology.

NAVFAC could not support some of its transactions because it did not have procedures in place to maintain supporting documentation. The DoD Financial Management Regulation<sup>15</sup> states that all documentation must be readily available for review by auditors and DoD Component's financial management personnel. The 17 unsupported transactions that totaled \$4,905 out of a sample value of \$373,083, included 13 transactions, valued at \$4,862, for Foreign National Labor.



NAVFAC lacked the procedures necessary to maintain supporting documentation.

While the dollar value of the unsupported transactions was not significant, the quantity of the unsupported transactions showed that NAVFAC lacked the procedures necessary to maintain supporting documentation. NAVFAC personnel explained that the foreign payroll office manually consolidated all personnel time and attendance for the command so that only paid dates and amounts remain. NAVFAC then manually entered the labor amounts into STARS-FL.

As a result, there was no direct link to trace the summary payment back to the individual's time and attendance report. The individual time and attendance amounts were included in our sample but did not have an identifier that traced the transaction through the system. As a result, a page by page search through all the transactions in the system as listed by the job order number was required to identify the sample transaction. In addition, the sample support provided included amounts and payment dates that were the same and could not be linked to an individual.

<sup>13</sup> Our sample from STARS-FL provided by Financial Management Office included transactions for Foreign National Labor, Reimbursable Work Order, CVP, and Supervision, Inspection, Overhead.

<sup>14</sup> We tested STARS-FL transactions processed by NAVFAC, STARS-HCM transactions processed by Office of Naval Research, and Navy ERP transactions processed by NAVAIR.

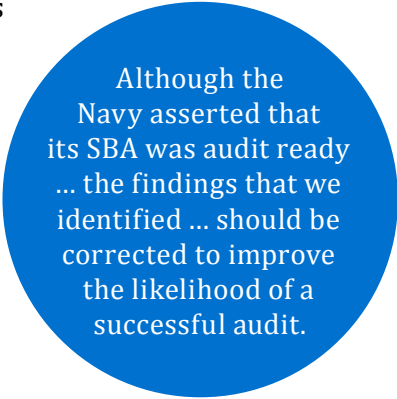
<sup>15</sup> DoD Regulation 7000.14-R, "DoD Financial Management Regulation," volume 4, chapter 9.

The 17 unsupported transactions also included four additional transactions: two Reimbursable Work Order, one CVP, and one Supervision, Inspection, Overhead transaction. Although NAVFAC provided some supporting documentation, it could not provide invoices that supported the transaction amounts. In addition, the amount for the Supervision, Inspection, Overhead transaction was changed; however, NAVFAC personnel could not provide documentation to show that the adjusted amount was correct.

As a result of these unsupported transactions, there is an increased risk that transactions are not valid and the financial statements are inaccurate. The Navy's SBA will include these transaction types and, if this condition is not corrected, the Navy's SBA may contain inaccurate account balances, which could have a negative impact on future Navy SBA audit opinions. In addition, the Navy would have a consistent process to reconcile and support its CVP amounts if standard operating procedures were in place. *The Deputy Assistant Secretary of the Navy (Financial Operations) should establish standard operating procedures to identify and retain supporting documentation for all transaction types. (Recommendation 3)*

## Navy's SBA Audit Opinion May Be At Risk

We determined Navy FMO could not provide a complete universe of CVP transactions. Specifically, Navy FMO did not complete reconciliations that would validate the CVP universe was accurate. In addition, some NAVFAC transactions were not supported, which could lead to inaccurate line-item balances. As Navy moves forward with its audit readiness efforts, determining that the financial statements contain all necessary transactions will be a key part of the financial statement audits. Although the Navy asserted that its SBA was audit ready based on assertions of business segments, including CVP, the findings that we identified in this report highlight specific challenges that should be corrected to improve the likelihood of a successful audit. If these deficiencies are not corrected, the Navy SBA audit opinion could be negatively affected.



Although the Navy asserted that its SBA was audit ready ... the findings that we identified ... should be corrected to improve the likelihood of a successful audit.

## Recommendations, Management Comments, and Our Response

We recommend that the Assistant Secretary of the Navy (Financial Management and Comptroller) (ASN(FM&C)):

### ***Recommendation 1***

**Develop a complete reconciliation process that is based on detail-level transaction data from Department of the Navy's general ledger systems that supports lines on the current Schedule of Budgetary Activity and other financial statements that the Navy may assert as audit ready.**

#### *Deputy Assistant Secretary of the Navy (Financial Operations) Comments*

The Deputy Assistant Secretary of the Navy (Financial Operations) responding for ASN (FM&C), agreed, stating that the Department of the Navy has implemented a reconciliation process that is based on detail-level transaction data from its general ledger systems that support lines on the current SBA. In addition, she stated the reconciliation process is currently being reviewed by an Independent Public Accountant as it conducts Navy's first financial audit of its FY 2015 SBA.

She also acknowledged that they were unable to provide a complete CVP transaction universe because of system limitations that did not allow for the identification and support of CVP transactions exclusive of other business segments. She stated that it is not in the Department of the Navy's best interest to identify transaction populations by business segment (CVP, RWO, etc.) because the efforts required to identify each transaction segment would require intense reconfiguration of the financial systems.

#### *Our Response*

The Deputy Assistant Secretary addressed all specifics of the recommendation, and no additional comments are needed. The intent of the recommendation will be met if the reconciliation process is reviewed by an Independent Public Accountant during the Navy's FY 2015 audit of the SBA.

## **Recommendation 2**

**Develop a process or system interface between Navy Enterprise Resource Planning and Wide Area Work Flow that provides timely processing of transactions. Update the DON's system business processes to ensure transactions are processed in compliance with the Statement of Federal Financial Accounting Standards 1.**

### *Deputy Assistant Secretary of the Navy (Financial Operations) Comments*

The Deputy Assistant Secretary of the Navy (Financial Operations), responding for ASN (FM&C), agreed, stating that the Navy developed a system interface between Navy ERP and WAWF that provides timely processing of transactions in compliance with Statement of Federal Financial Accounting Standards 1. However, the Deputy Assistant Secretary further stated that the liability recognition delay remains a limitation of the Navy ERP system because "Receipt and Acceptances" captured in WAWF still does not transfer as part of the interface. The Navy ERP user community drafted a Navy ERP Engineering Change Proposal in December 2012 to have that functionality added. The Engineering Change Proposal is awaiting implementation by the Naval Supply Systems Command Business Systems Center.

### *Our Response*

Comments from the Deputy Assistant Secretary partially addressed the recommendation. The Navy's Engineering Change Proposal for a system interface may provide a solution for the timely processing of transactions between Navy ERP and WAWF. However, the Navy did not provide specifics on how and when the Engineering Change Proposal would correct the liability recognition delay. We request that the Navy provide the Engineering Change Proposal and detailed narratives to demonstrate how the Engineering Change Proposal will correct the identified weakness and the planned completion date of these actions.

## **Recommendation 3**

**Establish procedures to identify and retain supporting documentation for all transaction types.**

### *Deputy Assistant Secretary of the Navy (Financial Operations) Comments*

The Deputy Assistant Secretary of the Navy (Financial Operations), responding for ASN (FM&C), agreed, stating that the Department of the Navy developed and issued policy in March 2012 on retaining documentation to support current and future Department of the Navy financial statement audits. The Deputy Assistant Secretary stated the policy directs the retention of documentation that supports financial statement beginning balances until the balances have been verified and accepted by the financial statement auditors.

### *Our Response*

Comments from the Deputy Assistant Secretary partially addressed the recommendation. The intent of our recommendation was to establish transaction identification and retention procedures, in the form of Standard Operating Procedures, throughout the Navy commands that would ensure all documentation needed to support financial statement balances at the transaction level was retained. These procedures would provide detailed steps an individual would take in order to retain supporting documentation of transactions processed at the command. Our audit identified that NAVFAC did not maintain and could not provide documentation to support individual transactions, which may be in contrast to the Navy's established policy from March 2012. We request that ASN (FM&C) provide additional comments to the final report that outlines the Navy's plan, including implementation dates, to establish documented procedures that will ensure documentation will be maintained at the command level for transactions supporting financial statement balances.



## Appendix A

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### Scope and Methodology

We conducted this performance audit from July 2014 through May 2015 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

We conducted site visits and interviewed Navy personnel at:

- Navy Financial Management Office in Washington, D.C.;
- NAVFAC in Washington, D.C.;
- Office of Naval Research in Washington, D.C.; and
- NAVAIR in Patuxent River, Maryland.

We discussed and reviewed supporting documentation for transactions. We reviewed the DoD Financial Management Regulation, Volume 10, Contract Payment Policy, to understand requirements related to the supportability of transactions. We also reviewed SFFAS 1, Accounting for Selected Assets and Liabilities, to determine the proper timing of liability recognition. In addition, we discussed the Navy's CVP business processes, reconciliations, and audit approach.

The Navy used three general ledger systems, STARS-FL, STARS-HCM, and Navy ERP, to process CVP transactions. We requested a CVP universe from the second quarter FY 2014 from each of these three systems; however, Navy officials could not provide a complete and reconcilable CVP universe from its three systems.

To select our sample for determining supportability of CVP transactions, we limited our review to those transactions in STARS-FL, STARS-HCM, and Navy ERP that were processed by NAVFAC, Office of Naval Research, and NAVAIR, respectively. We further limited the universe to transactions from U.S. General Ledger Account 4902 "Delivered Orders-Obligations, Paid," totaling \$2.4 billion, so that we could trace the transactions through the complete obligation and expenditure process. The universe was not accurate or complete to determine the total amount for the CVP universe.

To determine whether transactions were supported, we selected a nonstatistical random sample of 30 transactions from each of the three systems for a total of 90 sample items, with an absolute value of \$2.4 million. We obtained and reviewed supporting documentation for the sample items, which included commitment, obligation, and expenditure documentation.

## Use of Computer-Processed Data

We used computer-processed data from STARS-FL, STARS-HCM, and Navy ERP to determine whether the Navy's CVP transactions were auditable and supported. Specifically, we obtained all FY 2014 second quarter CVP transactions from STARS-FL, STARS-HCM, Navy ERP.

We tested reliability of the data by verifying if the universe was complete. To determine completeness we:

- obtained the CVP transaction universe from STARS-FL, STARS-HCM, and Navy ERP and interviewed Navy personnel to gain an understanding of the transaction universe;
- obtained and reviewed internal Navy standard operating procedures for pulling a Navy CVP universe;
- reviewed logic/methodology to determine how Navy provided us with transaction universe; and
- observed the process Navy uses to specifically identify CVP transactions.

We determined whether CVP posting logic was accurate by requesting posting logic to:

- identify CVP transactions;
- interview Navy personnel to gain an understanding of posting logic; and
- meet with Navy officials to determine internal processes related to determining logic in identifying CVP.

To validate the reconciliation process, we obtained:

- reconciliation standard operating procedures;
- a universe of CVP transactions from each system; and
- the system's unadjusted trial balances reconciliations.

We performed transaction testing for 90 transactions to determine whether transactions were supported. We obtained supporting documentation such as contracts, invoices, and Defense Finance and Accounting Services payment information to verify it was in compliance with guidance and consistent with the data in our sample transaction spreadsheet.

Based on our testing, we determined that:

- the CVP universe may be incomplete;
- Navy's posting logic was incorrect because segments other than CVP were identified;
- the reconciliations were not complete; and
- of the 90 transactions, 17 were unsupported and 30 were not processed timely.

The data reliability issues found are discussed in the finding section of the report.

## **Prior Coverage**

No prior coverage has been conducted on the Navy's CVP during the last 5 years.

## Appendix B

### Navy ERP Liability Recognition Delay

| Sample Number | Invoice Receipt Date | Liability Recognition Date | Difference Between Liability Date and Invoice Date | Transaction Amount |
|---------------|----------------------|----------------------------|--|--------------------|
| 1             | 2/4/2014             | 2/13/2014                  | 9  | \$386,765.37       |
| 2             | 2/12/2014            | 2/21/2014                  | 9  | \$6,838.13         |
| 3             | 2/14/2014            | 2/19/2014                  | 5  | \$27,185.45        |
| 4             | 3/13/2014            | 3/24/2014                  | 11   | \$7,665.07         |
| 5             | 12/20/2013           | 1/10/2014                  | 21   | \$9,591.00         |
| 6             | 1/21/2014            | 1/30/2014                  | 9  | \$75,102.52        |
| 7             | 1/7/2014             | 1/10/2014                  | 3  | \$1,443.00         |
| 8             | 12/3/2013            | 1/14/2014                  | 42   | \$12.24            |
| 9             | 3/6/2014             | 3/20/2014                  | 14   | \$1,439.47         |
| 10            | 1/2/2014             | 1/10/2014                  | 8  | \$34.04            |
| 11            | 2/7/2014             | 2/13/2014                  | 6  | \$75.57            |
| 12            | 2/10/2014            | 3/10/2014                  | 28   | \$15.92            |
| 13            | 1/10/2014            | 1/28/2014                  | 18   | \$2,597.14         |
| 14            | 11/27/2013           | 12/30/2013                 | 33   | \$2,703.99         |
| 15            | 1/8/2014             | 2/10/2014                  | 33   | \$23.69            |
| 16            | 1/22/2014            | 2/18/2014                  | 27   | \$5,318.94         |
| 17            | 2/10/2014            | 2/24/2014                  | 14   | \$14,325.00        |
| 18            | 12/18/2013           | 3/17/2014                  | 89   | \$7,536.42         |
| 19            | 2/12/2014            | 3/11/2014                  | 27   | \$15,262.61        |
| 20            | 12/20/2013           | 1/10/2014                  | 21   | \$63,110.18        |
| 21            | 2/20/2014            | 3/5/2014                   | 13   | \$31.30            |
| 22            | 1/6/2014             | 2/1/2014                   | 26   | \$626.49           |
| 23            | 12/31/2013           | 1/23/2014                  | 23   | \$31,318.84        |
| 24            | 2/21/2014            | 2/25/2014                  | 4  | \$845.32           |
| 25            | 12/4/2013            | 1/15/2014                  | 42   | \$6.12             |
| 26            | 12/18/2013           | 3/17/2014                  | 89   | \$585.20           |
| 27            | 1/28/2014            | 3/7/2014                   | 38   | \$3,006.48         |
| 28            | 1/16/2014            | 1/18/2014                  | 2  | \$1,691.81         |
| 29            | 1/7/2014             | 1/14/2014                  | 7  | \$30.60            |
| 30            | 2/11/2014            | 2/24/2014                  | 13   | \$21,251.42        |

## Management Comments

### Assistant Secretary of the Navy (Financial Management and Comptroller)



DEPARTMENT OF THE NAVY  
OFFICE OF THE ASSISTANT SECRETARY  
(FINANCIAL MANAGEMENT AND COMPTROLLER)  
1000 NAVY PENTAGON  
WASHINGTON, DC 20350-1000

22 June 2015


MEMORANDUM FOR INSPECTOR GENERAL OF THE DEPARTMENT OF DEFENSE

SUBJECT: Navy's Contract/Vendor Pay Process Was Not Auditable, Project

Reference: (a) DoDIG Draft Report (Project Number D2014-D000FS-0190.000)

In accordance with reference (a), the Office of Financial Operations has reviewed the subject draft report and provided the following comments in (attachment 1).

If you have any questions or concerns my point of contact for this matter is [REDACTED]

  
Karen L. Fenstermacher  
Deputy Assistant Secretary of the Navy  
(Financial Operations)

Attachment:  
As stated

cc:  
OUSD(C)  
DFAS



## Assistant Secretary of the Navy (Financial Management and Comptroller) (cont'd)

DEPARTMENT OF DEFENSE INSPECTOR GENERAL DRAFT REPORT DATED 07 MAY 2015

PROJECT NUMBER D2014-D000FS-0190.000

### "NAVY'S CONTRACT/VENDOR PAY PROCESS WAS NOT AUDITABLE"

DON RESPONSE: CONCUR. The Department of the Navy (DON) concurs with the recommendation to develop a complete reconciliation process that is based on detail-level transaction data from DON's general ledger systems that supports lines on the current Schedule of Budgetary Activity (SBA) and other financial statements that the Navy may assert as audit ready. The DON has implemented a reconciliation process that is based on detail-level transaction data from its general ledger systems that support lines on the current SBA. This reconciliation process is currently being reviewed by an Independent Public Accountant (IPA) as it conducts Navy's first financial audit of its FY15 SBA.

Navy acknowledges that it was unable to deliver a complete Contract Vendor Pay (CVP) transaction universe due to system limitations that did not allow for the identification and support of CVP transactions exclusive of other segments. CVP transactions were not able to be successfully disaggregated from all Reimbursable Work Order (RWO) transactions. The Office of Financial Operations (FMO) determined that it is not in the Navy's best interest to continue to identify transaction populations and reconcile them by business segment (CVP, RWO, etc.) as the effort to ensure all Navy financial systems are able to specifically identify each transaction to a segment would require intense reconfiguration of these systems. Also, the Navy believes that an auditor will want to see transactions reconciled from the Financial Statement Line item level to the General Ledger accounts that make up those accounts. This being the case, the Navy will concentrate its reconciliation efforts at the Financial Statement level for its Full Financial Statement Audit Readiness effort and does not see the benefit in completing a large scale effort that enables the Navy to reconcile transactions at the business segment level.

DON RESPONSE: CONCUR. The DON concurs with the recommendation to develop a process or system interface between Navy Enterprise Resource Planning (ERP) and Wide Area Work Flow (WAWF) that provides timely processing of transactions. The DON also concurs with the recommendation to update DON system business processes to ensure transactions are processed in compliance with Statement of Federal Accounting Standards 1. The DON currently has an implemented system interface between Navy ERP and WAWF, but only when the vendor submits the invoice in WAWF and Navy ERP is the entitlement system (internal entitlement). Otherwise, the liability recognition delay is a limitation in the Navy ERP system because at this time, the required "Receipts and Acceptances" captured in WAWF does not interface to Navy ERP. The Navy ERP user community drafted and submitted to FMO a Navy ERP Engineering Change Proposal (ECP) in December 2012 to have that functionality added to the WAWF interface program; this ECP is currently awaiting implementation by the NAVSUP Business Systems Center (BSC).

DON RESPONSE: CONCUR. The DON concurs with the recommendation to establish procedures to identify and retain supporting documentation for all transaction types. In March 2012, the DON issued policy and guidance on retaining documentation to support current and future DON financial statement audits. The policy directs the continued retention of all documentation that support financial statement beginning balances until beginning balances on the DON financial statements have been verified and accepted by the financial statement auditors. The policy further states that the Audit Response Center (ARC) was established to manage Provided by Client (PBC) list items and other auditor document requests.

## Acronyms and Abbreviations

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|                  |   |
|------------------|---|
| <b>CVP</b>       | Contract/Vendor Pay   |
| <b>NAVAIR</b>    | Naval Air Systems Command   |
| <b>NAVFAC</b>    | Naval Facilities Engineering Command                                      |
| <b>Navy ERP</b>  | Navy Enterprise Resource Planning   |
| <b>FMO</b>       | Office of Financial Operations  |
| <b>SBA</b>       | Schedule of Budgetary Activity  |
| <b>SFFAS</b>     | Statement of Federal Financial Accounting Standards                       |
| <b>STARS-FL</b>  | Standardized Accounting and Reporting System-Field Level                  |
| <b>STARS-HCM</b> | Standardized Accounting and Reporting System-Headquarters Claimant Module |
| <b>WAWF</b>      | Wide Area Workflow  |



# **Whistleblower Protection**

## **U.S. DEPARTMENT OF DEFENSE**

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